EASTERN PROVINCIAL AIRWAYS

Ken

Annual Report 1975

EASTERN PROVINCIAL AIRWAYS LIMITED
and Subsidiary Companies

OFFICERS

Andrew Chesley Crosbie,
Chairman of the Board

Arthur James Lewington,
Deputy Chairman of the Board

Keith Alfred Miller,
President and Chief Executive Officer

William Farrell Gaudet,
Vice President Administration

William Henry Harris,
Vice President Government and Community Relations

Bryan Goodwin Jones,
Vice President Operations

Marshall Bruce Jones
Vice President Affiliated Companies

Harold Raymond Steele
Vice President Traffic & Sales

Harold Lewis Wareham
Vice President Finance & Planning & Secretary

HEAD OFFICE

Gander International Airport,
Gander, Newfoundland

BANKERS

The Royal Bank of Canada, Gander, Nfld.
The Mercantile Bank of Canada, Montreal, P.Q.

AUDITORS

Peat, Marwick, Mitchell & Co.,
Chartered Accountants,
St. John's, Newfoundland

LEGAL COUNSEL

Herridge, Tolmie,
Ottawa, Ontario
Johnston, Heenan & Blaikie,
Montreal, P.Q.
Alyward & Crosbie,
St. John's, Newfoundland

TRANSFER AGENT & REGISTRAR

The Royal Trust Company,
St. John's, Halifax, Montreal,
Toronto, Winnipeg, Regina, Calgary

STOCK LISTING

The Toronto Stock Exchange
The Montreal Stock Exchange

DIRECTORS

Andrew Chesley Crosbie,
President & Chief Executive Officer,
Newfoundland Engineering and Construction Co. Ltd.,
St. John's, Nfld.

Arthur James Lewington,
Deputy Chairman of the Board,
Eastern Provincial Airways

**Keith Alfred Miller,
President & Chief Executive Officer,
Eastern Provincial Airways

Harold Anthony Collins,
Minister of Health,
Province of Newfoundland & Labrador

Walter John Cox,
President, The Pure Milk Co. Ltd.,
Charlottetown, P.E.I.

John M. Coyne,
Partner, Herridge, Tolmie,
Ottawa, Ontario.

*William Farrell Gaudet,
Vice-President, Administration,
Eastern Provincial Airways

Richard Greene,
Partner,
Greene, McNab & Baird, St. John's, Nfld.

Arthur Russell Harrington,
Vice-President, Halifax Developments Ltd.,
Halifax, N.S.

*William Henry Harris,
Vice-President, Government & Community Rels.
Eastern Provincial Airways

*Bryan Goodwin Jones,
Vice-President, Operations,
Eastern Provincial Airways

*Marshall Bruce Jones,
Vice-President, Affiliated Companies,
Eastern Provincial Airways

Richard Henry Oland,
Officer, Moosehead Breweries Limited,
Saint John, N.B.

Harold Raymond Steele,
Vice-President, Traffic & Sales,
Eastern Provincial Airways

*Harold Lewis Wareham,
Vice-President, Finance & Planning & Secretary,
Eastern Provincial Airways

*Members of the Executive Committee
**Chairman of the Executive Committee

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EASTERN PROVINCIAL AIRWAYS LIMITED
and Subsidiary Companies

Comparative Highlights

	1975	1974
Earnings		
Revenues - Gross	$35,902,000	$30,823,000
Net (Loss) Earnings	$ (190,000)	$ 506,000
(Loss) Earnings per Common Share - Basic	$ (0.27)	$ 0.37
Average Common Shares Outstanding	1,201,915	1,201,175
Financial Position		
Working Capital	$ 1,133,000	$ 1,616,000
Property and Equipment - Net	$22,808,000	$22,560,000
Long-Term Debt	$17,643,000	$17,375,000
Shareholders' Equity	$ 7,464,000	$ 6,799,000
Equity per Common Share	$ 4.59	$ 4.83
Operating Statistics		
Passengers Carried	604,000	594,000
Cargo Ton Miles	3,799,000	3,810,000
Revenue Ton Miles	27,575,000	27,666,000
Capacity Ton Miles	51,532,000	52,053,000
Revenue Weight Load Factor	53.5%	53.2%

Directors' Report to the Shareholders

It is now a matter of record that 1975 resulted in very severe strains being placed upon the scheduled airline industry in Canada. The softening demand for air transportation coupled with escalating fuel and labour costs caused many of the scheduled airlines in the country to incur losses. In the case of Eastern Provincial Airways, the Airline suffered its first loss since entering the jet age in 1969.

Forecasts prepared early in the year indicated that an upturn in the economy could be forthcoming by mid-year. However, results in the first two months indicated that conditions were in fact deteriorating rather than levelling off. Accordingly, the Airline management moved speedily to reduce capacity offered on scheduled services and to provide additional capacity on charter services where demand continued to increase. As a result of these actions the Airline was able to maintain a load factor which was marginally better than that maintained in 1974. This was achieved even though delivery of our seventh Boeing 737 jet aircraft was made in November of 1975. Revenues from all sources in 1975 amounted to \$35,902,000 compared with \$30,823,000 in 1974. This constitutes an increase of 16%. Operating costs in 1975 totalled \$32,222,000 compared with \$26,282,000 in 1974. This constitutes an increase of 23%. The foregoing adverse trend is one which plagued most Airlines throughout the world.

The increase in revenue is not attributable in any way to an increase in the number of scheduled passengers carried. In fact, there were 604,000 scheduled passengers carried in 1975 compared to 594,000 in 1974. This was a marginal increase of 10,000 scheduled passengers throughout the entire system. The increase in total revenue is attributable primarily to two factors: increased revenues resulting from a general passenger fare increase of approximately 10% which became effective in late May of 1975; an increase of a little in excess of \$2,000,000 resulting from expanded charter activities to southern destinations.

The deterioration in demand for air travel was aggravated further by public service strikes which had a very adverse effect on our revenue. Early in the year Federal Airport Employees embarked on a series of rotating strikes which had the effect of virtually closing down two pivotal points on our system — Halifax, N.S., and Goose Bay, Labrador. The strike of Postal employees caused the Airline to lose a substantial amount of mail revenue.

The efforts of the Airline management to reduce costs were stepped up again in the fall of the year when scheduled capacity was again reduced resulting in the lay-off of a large number of employees. These actions contributed to the gaining of a reasonable load factor along with a cost structure that was tailored to meet the

capacity demands which were being placed on the Airline.

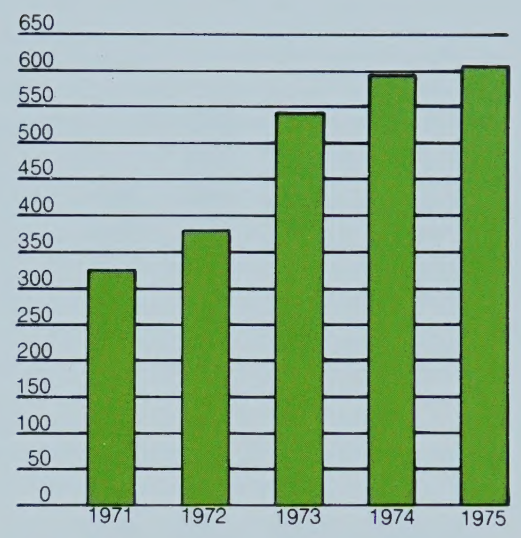
Included in total revenue of $35,902,000 is an amount of $1,700,000 paid to the Airline for the provision of air services over specific routes which are uneconomic. The Government of Canada froze this subsidy at $1,700,000 during 1975. This amount was insufficient to reimburse the Company for the actual losses incurred in providing the socially necessary services on the routes which had been specifically designated as eligible for Federal subsidy payment. The losses incurred by the Airline in providing services on these routes total $2,289,057 which results in a shortfall to the Airline of $589,000. The Airline has been advised by the Canadian Government that during 1976 subsidy payments will be frozen again at the same level as 1975. The Airline has under preparation an appeal of this decision. If the Airline fails to win this appeal then immediate consideration will be given to a curtailment of the services offered on subsidy eligible routes.

The net loss for the year amounted to $190,000 or 27c per common share compared with net earnings of $506,000 or 37c per common share for 1974. Included in these earnings is an amount of $22,000 after taxes earned by the Airline's hotel subsidiary. These hotel earnings constitute earnings of 2c per common share. In respect of financial statistics, it is significant to note that funds generated from operations during 1975 were approximately $3,000,000 below funds generated in each of the previous four years.

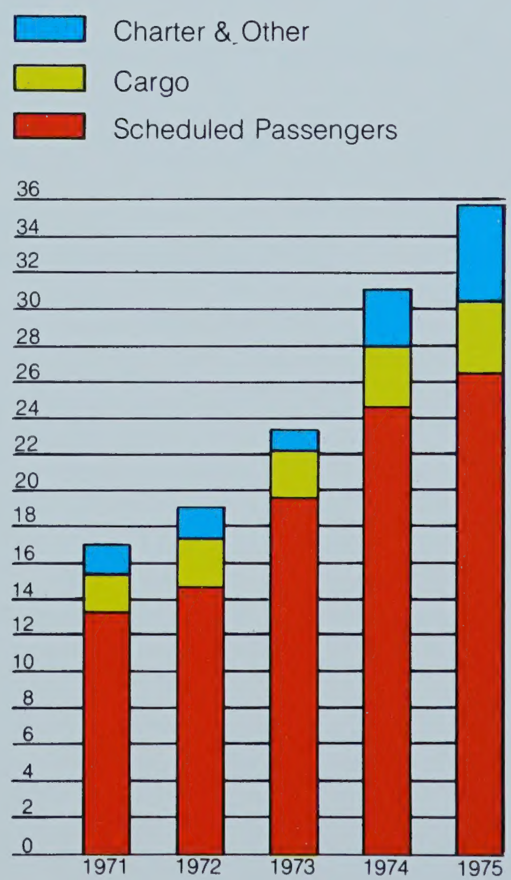
It has been stated earlier that during 1975 the Company embarked on two programs of capacity curtailment as well as a program of cost reductions including employment lay-offs. However, further decisions were required in order for the Company to maintain reasonable working capital levels. In June a Boeing 737 aircraft was refinanced through a sale and lease-back arrangement. This refinancing improved working capital by an amount in excess of $1,500,000 and gave rise to a gain of $424,000 after provision for deferred income taxes. A further improvement in working capital was achieved by the issuance of $1,020,000 series 'B' 10¾% redeemable preferred shares. To preserve working capital further no dividends were declared or paid on common shares after January 1, 1975.

In the last Annual Report as well as in Quarterly Reports issued throughout the year, the Company provided detailed information on the financing and progress of the Flight Training Centre to be located in Halifax, Nova Scotia and the expansion to the Engineering and Maintenance Facility in Gander, Newfoundland. Work on both projects is on schedule and within the capital cost budget. It is expected that we will be moving personnel into the Halifax Facility during the late fall of this year and

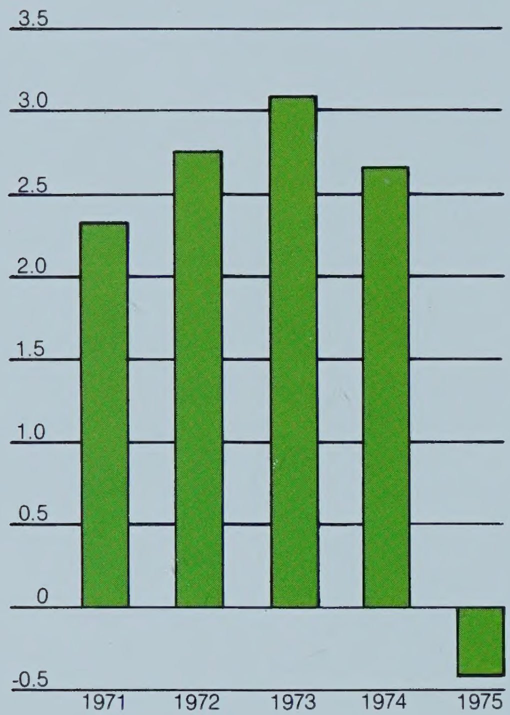
PASSENGERS CARRIED
(THOUSANDS)



REVENUE
(MILLIONS)



FUNDS GENERATED FROM OPERATION
(MILLIONS)



that the simulator facility itself will be operational by the spring of 1977. The Gander Expansion Program will be completed and completely operational by year-end.

The plans of the Airline to undertake its own heavy airframe maintenance are proceeding ahead of schedule and in fact some of this work has been commenced already on certain specific jet aircraft.

During April of 1975 the Airline inaugurated its two new jet services over the routes Halifax - Fredericton - Montreal and Halifax - Saint John - Montreal. To coincide with this Air Canada inaugurated its services between Toronto - Ottawa and Charlottetown. Traffic on our new routes was disappointing and the revenue was not sufficient to reimburse the Airline its revenue losses resulting from the introduction of Air Canada services to Prince Edward Island. The Airline entered the market as a new carrier at a time when conditions were most unfavourable in the economy. The marketing personnel of the Airline have continued with an aggressive sales program and within the last two months indications are that by the summer we will have satisfactory load factors on both of these routes.

The air service to St. Anthony, Newfoundland, operated by a DC-3 aircraft was terminated in September of the year when service was provided by a third level carrier. Termination of this service allowed the Airline to sell its one remaining DC-3 aircraft. However, the Airline still operates one only DC-3 aircraft between Sydney, Nova Scotia and St. Pierre and Miquelon, France. The Airline has before the Canadian Transport Commission an application to upgrade this service from piston engine DC-3 equipment to Hawker Siddeley 748 turbo-prop equipment. When and if this approval is received the Airline will end an era in that it will no longer operate piston engine aircraft. In order to provide for this service as well as to provide a back-up HS748 aircraft for existing mainland turbo-prop services, the Airline leased a second Hawker Siddeley 748 aircraft on a long-term basis in December of 1975.

It has been reported in previous reports that the Airline has applied to the Canadian Transport Commission to provide services to a large number of smaller points in Atlantic Canada. Although this application has been advertised publicly by the Canadian Transport Commission, no date has been set for a public hearing at the time of this writing. The Airline was gratified, however, by the very large number of interventions placed before the Commission in support of the application.

During the last quarter of the year the Company completed negotiations for the acquisition of 75% of the outstanding common shares of a wholesale tour company based in Halifax, Nova Scotia. It is the intention of the Airline to utilize the tour company as a means of

providing cheap vacations in the southern sunspots for the residents of Atlantic Canada and also to give some measure of control over the utilization of the Airline's jet fleet in charter activities to the South. The Company was purchased as part of a longterm plan and it is not expected that the tour operation will make any profits during 1976 since that year primarily will be an organizational year.

During 1973 collective labour agreements were signed with all unions and associations representing the Company's employees. All of these contracts expired during 1975. New agreements have now been re-negotiated and signed with the pilots, engineering and maintenance personnel, traffic and reservations agents and clerical personnel. Just prior to year-end a wage settlement was signed with the flight dispatch group. The sole contract awaiting completion is with the Airline's Flight Attendants and these negotiations are now at the conciliation level. The Airline is subject to the rules and regulations of the newly constituted Anti-Inflation Board.

The downturn in demand for air travel caused by recessionary influences was aggravated further by the deferral of the Lower Churchill Hydro Electric Development in Labrador. The first two months of 1976 indicated that the downward trend was continuing. However, during the past month there has been a very definite upturn in demand for seats on the system of Eastern Provincial and your management believes now that if this trend continues we can forecast an improvement in operating results for 1976. Factors which will contribute to an improvement in financial results will include the recent general passenger fare increase of approximately 9% which is to become effective on May 9th and the signing of a lease agreement for the lease of a Boeing 737 jet aircraft to Wien Air Alaska for a six month period from May 1st to October 31st, 1976. Additionally, the Airline has re-negotiated and increased the charter rates applicable to all flights into the Bahamas which will be operated for a major tour wholesaler during the fall of 1976 and spring of 1977. Consequently, in spite of all the adverse effects experienced during the past year, the Company believes that the indicated upturn in demand and recent managerial action with respect to costs, fares and aircraft utilization will enhance more favourable economic results during 1976. To further strengthen working capital as a result of the losses incurred during the first two months of 1976, the Airline refinanced a Boeing 737 jet aircraft during late March of this year. The refinancing of the aircraft through a sale and lease-back arrangement improved working capital by an amount in excess of $2,000,000 and gave rise to a gain in excess of $600,000 after provision for deferred income taxes.

It is the belief of your Company that the Airline must be awarded additional longhaul routes in order to provide for a sounder economic base in its operations. This is because your Airline operates with an average stage distance which is lower than any experienced by any major scheduled air carrier in Canada. Moreover, the average unit revenue yield is the lowest of any Regional Air Carrier in Canada. The highest costs are associated with the lowest stage distances. As a result of this we operate with high costs and yet appear to obtain very low average yields. Of particular interest to the Company are longer haul air routes within Atlantic Canada as well as greater access to the Montreal market from Atlantic Canada. It is the contention of your Airline that it is deserving of these route awards because of the relatively large number of shorthaul services that it is required to provide within the Atlantic Provinces.

The devotion to duty of all Airline employees during 1975 was again exemplary. The Airline, therefore, expresses its deep gratitude to all personnel for the contributions made during a very difficult year.

On behalf of the Board of Directors.

K. A. Miller

K. A. Miller,
President & Chief Executive Officer.

Consolidated Statement of Earnings

YEAR ENDED DECEMBER 31, 1975
with comparative figures for 1974
(expressed in thousands of dollars)

	1975	1974
Revenues		
Scheduled operations	$28,974	26,187
Government subsidies - Note 8	1,700	1,725
Charter and other	5,228	2,911
	35,902	30,823
Expenses		
Operating, including provision for major engine overhauls - Note 9	34,769	28,050
Depreciation and amortization	1,762	1,352
	36,531	29,402
(Loss) earnings from operations	(629)	1,421
Other income, including gain on sale of property and equipment - Note 7 (b)	1,553	484
	924	1,905
Interest and debt expense		
Long-term debt, less sinking fund earnings	1,377	972
Other	79	85
	1,456	1,057
(Loss) earnings before deferred income taxes	(532)	848
Deferred income taxes - Note 5	342	(342)
Net (loss) earnings for the year	$(190)	506
(Loss) earnings per common share		
Basic - Notes 7 (b) and 9	$(0.27)	0.37

See accompanying notes to consolidated financial statements

EASTERN PROVINCIAL AIRWAYS LIMITED
and Subsidiary Companies

Consolidated Statement of Changes in Financial Position

YEAR ENDED DECEMBER 31, 1975
with comparative figures for 1974
(expressed in thousands of dollars)

	1975	1974
Funds applied to		
Net loss for the year	$ 190	
Items not involving funds for the year - net	215	
Funds applied to operations	405	
Property and equipment	11,434	8,333
Long-term debt	6,310	1,812
Dividends	137	300
Sinking fund investments	298	296
Investments and deferred charges	742	131
Purchase for cancellation of Series A Preferred shares - Note 6	31	-
Total funds applied	19,357	10,872
Funds provided by		
Net earnings for the year		506
Items not involving funds for the year - net		2,148
Funds provided from operations		2,654
Transfer of property to "Asset held for disposal" - Note 2	1,605	352
Sale of property and equipment - Note 7 (b)	9,370	395
Long-term borrowings	6,876	6,829
Issue of capital stock - Note 6	1,023	-
Total funds provided	18,874	10,230
Decrease in working capital	483	642
Working capital as of beginning of year	1,616	2,258
Working capital as of end of year	$ 1,133	1,616

See accompanying notes to consolidated financial statements

Assets

	1975	1974
Current assets		
Cash and term deposit	$ 639	1,537
Short-term investments, at cost (market value $777; 1974 - $581)	868	634
Receivables - Notes 7 (b), 7 (e) and 8	5,405	4,092
Materials, supplies and parts, at lower of cost or net realizable value	1,312	1,044
Asset held for disposal - Note 2	1,605	372
Prepaid expenses	179	320
Total current assets	10,008	7,999
Investments, at cost	1,132	870
Property and equipment, at cost		
Flight equipment	23,215	22,431
Buildings and ground facilities	3,119	3,620
	26,334	26,051
Less accumulated depreciation and provision for overhaul of owned aircraft engines	3,526	3,491
Net property and equipment	22,808	22,560
Deferred charges - Note 3	836	488
Excess of cost of investment in shares of subsidiary over equity in net assets at date of acquisition	1,856	1,856
	$36,640	33,773

See accompanying notes to consolidated financial statements

Consolidated Balance Sheet

DECEMBER 31, 1975
with comparative figures for 1974
(expressed in thousands of dollars)

Liabilities and Shareholders' Equity

	1975	1974
Current liabilities		
Bank indebtedness, secured by a general assignment of a subsidiary's receivables	$ 1,630	1,034
Accounts payable and accrued liabilities	4,121	2,614
Current portion of long-term debt - Note 4	2,102	1,812
Dividends payable	14	75
Deferred revenue	1,008	848
Total current liabilities	8,875	6,383
Long-term debt - Note 4	17,643	17,375
Provision for overhaul of leased aircraft engines	474	690
Deferred income taxes - Note 5	2,184	2,526
Shareholders' equity - Note 6		
Capital stock	3,433	2,455
Contributed surplus	14	-
Excess of appraised value of property and equipment over cost	-	203
Retained earnings	4,017	4,141
Total shareholders' equity	7,464	6,799
Commitments and contingent liabilities - Notes 2 and 7		
	$36,640	33,773

ON BEHALF OF THE BOARD:

K. A. Miller (Signed) .... DIRECTOR

H. L. Wareham (Signed) .... DIRECTOR

EASTERN PROVINCIAL AIRWAYS LIMITED
and Subsidiary Companies

Consolidated Statement of Retained Earnings

YEAR ENDED DECEMBER 31, 1975
with comparative figures for 1974
(expressed in thousands of dollars)

	1975	1974
Retained earnings as of beginning of year	$ 4,141	3,924
Net (loss) earnings for the year	(190)	506
Realization of excess of appraised value of property and equipment over cost	203	11
	4,154	4,441
Dividends		
Preferred shares - Series A	58	60
- Series B	79	-
Common shares	-	240
	137	300
Retained earnings as of end of year	$ 4,017	4,141

See accompanying notes to consolidated financial statements

AUDITORS' REPORT TO THE SHAREHOLDERS

We have examined the consolidated balance sheet of Eastern Provincial Airways Limited and subsidiaries as of December 31, 1975 and the consolidated statements of earnings, retained earnings and changes in financial position for the year then ended. Our examination included a general review of the accounting procedures and such tests of accounting records and other supporting evidence as we considered necessary in the circumstances.

In our opinion, the accompanying consolidated financial statements present fairly the financial position of the Company and its subsidiaries as of December 31, 1975 and the results of their operations and changes in their financial position for the year then ended, in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

Peat, Marwick, Mitchell & Co.
Chartered Accountants

St. John's, Newfoundland
March 16, 1976

1. Summary of Significant Accounting Policies

(a) Basis of consolidation

The consolidated financial statements include the accounts of Eastern Provincial Airways Limited (the Company) and its wholly-owned subsidiary companies, Maritime Central Airways Limited (Maritime Central), Eastern Provincial Airways (1963) Limited (Eastern Provincial), and Atlantic Inns Limited (Atlantic). The "Excess of cost of investment in shares of subsidiary over equity in net assets at date of acquisition" amounting to $1,855,620 arose upon the acquisition of Maritime Central.

(b) Depreciation

Depreciation on property and equipment is provided at straight-line rates which are related to the estimated useful lives of the assets which are as follows:

	Useful Life	Residual Value
Jet aircraft and spare parts	14 years	15%
Propeller aircraft and spare parts	10 years	10%
Buildings	20 years	-
Ground facilities	5 years	-

(c) Capitalization of interest

Interest is capitalized on expenditures related to the acquisition of property and equipment before such assets are placed in service. Such capitalized interest is amortized over the useful lives of the related assets.

(d) Aircraft maintenance

Engines - Provision for major overhauls of owned and leased aircraft engines which are performed by outside agencies is made based on aircraft flying time at rates per hour computed in relation to the estimated costs of the overhauls.

Airframes - Maintenance of airframes is performed on a continual in-house basis and accordingly is expensed when incurred.

(e) Amortization

Deferred charges are amortized on a straight-line basis over five years with the exception of deferred financing expenses which are amortized over the terms of the related financing.

(f) Revenue recognition

The recognition of revenue is deferred until the related services are rendered. Prepayments of such services as of the year end are included under "Deferred revenue".

(g) Foreign currency translation

Current balances receivable and payable in foreign currencies have been translated to Canadian dollars at the exchange rates prevailing as of the balance sheet date. Non-current balances originating in foreign currencies have been translated at historical rates of exchange.

(h) Income taxes

Income taxes are accounted for on the tax allocation basis in recognition of the income tax liability deferred when deductions that are claimed for income tax purposes are greater than corresponding expenses recorded in the accounts.

(i) Earnings per common shares

Basic earnings per share information has been computed using the weighted average number of Common shares outstanding during the year.

2. Asset Held For Disposal

During 1975 Eastern Provincial commenced construction of an extension to its Gander hangar facility at an estimated total cost of $1,200,000 of which $261,000 was expended during the year. The Province of Newfoundland has confirmed in writing that it "will arrange financial assistance in a manner so as to ensure that the building will be sold by Eastern Provincial Airways and bought by either the Province, an agent of the Province or some external party, and the proceeds will be received in 1976, for a price not less than the net book value of the facility."

Accordingly, $1,605,672 representing the net book value of the facility at December 31, 1975, is included in current assets under "Asset held for disposal".

3. Deferred Charges

Deferred charges are carried in the balance sheet at cost less accumulated amortization and are summarized as follows:

	1975	1974
Training expenses	$243,073	234,699
Financing expense	362,409	253,422
Crew transfer expenses	230,908	-
	$836,390	488,121

4. Long-Term Debt

	1975	1974
$6^1/_2$% sinking fund debentures due March 15, 1991 (less sinking fund investments $3,868,000, (1974 - $3,570,000))	$ 2,132,000	2,430,000
8% conditional sale agreement, repayable in blended quarterly instalments of $178,000 to October 29, 1983	4,197,344	9,147,761
Bank loan, at prime plus 1%, repayable in equal quarterly instalments to December 31, 1976 and a final payment of $300,000 due in 1977	540,000	780,000
6% term loan repayable in 10 equal semi-annual instalments commencing July 10, 1980 guaranteed by a Canadian bank holding a chattel mortgage on an aircraft	2,562,246	2,479,182
Bank loan, at prime plus $2^1/_8$%, repayable in 10 equal semi-annual instalments to December 31, 1979 secured by a chattel mortgage on an aircraft	3,120,000	3,900,000
8% term loan, repayable in 8 semi-annual instalments commencing May 10, 1982, guaranteed by a Canadian bank holding a chattel mortgage on an aircraft	2,211,043	-
Bank loan, at prime plus 2%, repayable in 25 quarterly instalments of $162,500 to March 31, 1982, and a final payment of $137,500 on June 30, 1982, secured by a chattel mortgage on an aircraft	4,200,000	-
Current obligations to be repaid from proceeds of long-term financing	382,246	-
Bank loan, at prime plus 2%, repayable in blended monthly instalments of $8,309 each to December 31, 1981, secured by a collateral mortgage on real property	400,198	450,000
	19,745,077	19,186,943
Less portion due within one year included in current liabilities	2,102,156	1,811,744
Net long-term debt	$17,642,921	17,375,199

The sinking fund debentures are unconditionally guaranteed by the Province of Newfoundland; this guarantee being secured by a first and specific mortgage on certain assets and a first floating charge on certain other assets. The sinking fund investments together with future earnings of the fund will be sufficient to retire the principal amount of the sinking fund debentures at maturity.

In accordance with the terms of the 8% conditional sale agreement under which delivery was accepted of a Boeing 737 jet aircraft and related spare parts, the rights, titles, and interest in the equipment have been assigned and transferred to the lender until such time as the financing under the agreement has been repaid. In addition debentures amounting to $600,000, included in the accompanying balance sheet under "Investments", have been pledged to the lender.

In connection with certain loan and lease agreements the Company has agreed to maintain on a consolidated basis a minimum net worth, as defined, of $7,000,000, and Eastern Provincial has agreed, among other things, to:

(i) Maintain a minimum working capital, as defined, of $1,000,000;

(ii) Not declare or pay dividends in any one year in excess of 50% of its net earnings for the previous year; and,

(iii) Not make capital expenditures in excess of $500,000 in any one year without prior written consent of the lessor and lender.

Maturities on long-term debt other than $6^1/_2$% sinking fund debentures for the five years ending December 31, 1976 through 1980 amount to $2,102,156, $2,207,459, $1,957,616, $2,010,971 and $1,533,502.

5. Deferred Income Taxes

The deferred tax liability as of December 31, 1975 relates chiefly to the excess of capital cost allowance claimed for tax purposes over depreciation recorded in the accounts.

6. Capital Stock

	1975	1974
Preferred shares of $15 par value each, issuable in series. Authorized - 135,000 shares. Series A - 6% cumulative, redeemable, convertible Preferred shares. Authorized 67,000 shares; issued 63,440 shares (1974 - 66,450)	$ 951,600	996,750
Series B - 10¾% cumulative, redeemable Preferred shares. Authorized 68,000 shares; issued 68,000 shares (1974 - nil)	1,020,000	-
Deferred shares of $100 par value each. Authorized 47,500 shares; issued and eliminated on consolidation 24,964 shares	-	-
Common shares without nominal or par value. Authorized 3,000,000 shares; issued 1,202,495 shares (1974 - 1,201,475)	1,461,125	1,458,325
Total capital stock	$ 3,432,725	2,455,075

Pursuant to the redemption conditions attaching to the Series A Preferred shares the Company is required to apply each year to the purchase for cancellation of these shares an amount equal to three percent of the aggregate par value of Series A Preferred shares outstanding at the end of the preceding year. During 1975, an amount of $31,327 was applied to the purchase for cancellation of 3,000 shares with an aggregate par value of $45,000. In accordance with Section 49 of the Companies Act, Newfoundland the amount of $45,000 has been appropriated from retained earnings as a "capital redemption reserve fund" which may not be reduced or converted, except in accordance with the provisions of the Act. The excess of the par value of the shares redeemed over the purchase price has been included under "Contributed Surplus".

Series A Preferred shares are convertible into Common shares at the option of the shareholder on the basis of two Common shares for each Series A Preferred share. Pursuant to this conversion privilege, 20 Common shares were issued during 1975 and 126,880 Common shares are reserved for issuance as of December 31, 1975 (1974 - 132,900). A further 99,000 Common shares are reserved for issuance to employees (other than present directors and officers) under a Stock Option Plan and a Stock Purchase Plan created in 1972. In 1974, share options were granted to employees under the Stock Option Plan to purchase 33,000 Common shares on or before December 12, 1979 at an exercise price of $2.65 per share. Pursuant to this plan, 1,000 Common shares were issued during 1975 and options for 31,500 Common shares remained unexercised as of December 31, 1975. No shares have been offered under the Stock Purchase Plan as of December 31, 1975.

During the year the Company issued 68,000, 10¾% Series B cumulative, redeemable, Preferred shares at a par value of $15 each, for an aggregate consideration of $1,020,000. Pursuant to the redemption conditions attaching to these shares, the Company is required to redeem, at par value, during the five years ending April 15, 1976 to 1980, 3,400 shares, 6,800 shares, 6,800 shares, 10,200 shares and 40,800 shares respectively.

7. Commitments and Contingent Liabilities

(a) On December 29, 1971, Eastern Provincial sold three Boeing 737 jet aircraft and a spare engine and entered into an agreement whereby the three aircraft and spare engine were leased back for a period of thirteen years at a basic annual rental of $1,702,380.

As part of this transaction, the Company and certain of its subsidiaries have agreed to indemnify a third party in respect of a loan of $10,500,000 (loan balance as of December 31, 1975 - $8,373,000) made to the purchaser of the three above mentioned aircraft, and in addition have agreed to indemnify the guarantor of the loan. To secure this indemnification the Company and certain of its subsidiaries have executed a specific mortgage on certain assets and a floating charge on all other assets, except those assets which may be given as security for bank loans. The mortgage is subordinated to the first and specific mortgage relating to the 6½% sinking fund debentures included in long-term debt.

(b) In June, 1975, Eastern Provincial sold one Boeing 737 jet aircraft as well as a spare engine and certain spare parts. The aircraft has been leased back for a period of ten years at a basic annual rental of $826,000, and the spare engine and spare parts for a period of seven years and nine months at a basic annual rental of $55,270.

During the year Eastern Provincial purchased two Hawker Siddely HS-748 aircraft which were sold and leased back for periods of approximately twelve years and nine years at basic annual rentals of $182,613 and $174,493 respectively. $967,500 of the

sale price was not received until January 1976 and is included in current assets under "Receivables".

The gains totalling $965,699 realized from the sale of the three aircraft are included in the statement of earnings under "Other income" and has served to reduce the basic loss per Common share by $0.38.

(c) On February 5, 1975, Eastern Provincial entered into a preliminary agreement to purchase three DHC-7 aircraft for delivery during 1977, at a basic purchase price totalling $7,753,000. Deposits of $25,000 per aircraft have been made, which are refundable should a final purchase contract not be executed.

(d) During 1974 Eastern Provincial received a Federal Sales Tax assessment in the amount of $561,899 relating to the purchase and importation of one Boeing 737 jet aircraft on October 29, 1973. Counsel has advised that this assessment is not justified in law and consequently Eastern Provincial has disputed this assessment and maintains that no part of this amount is, or will become, payable. Accordingly, no provision has been made for this amount in the accounts.

(e) During 1975, Eastern Provincial commenced construction of an aircraft hangar at Halifax at an estimated total cost of $4,100,000, for which agreements have been signed with an agency of the Province of Nova Scotia for long-term financing of up to $4,065,000 at an interest rate of 11%. To December 31, 1975, approximately $280,000 has been expended on this project.

Related to this project, Eastern Provincial has undertaken to establish a training facility, including the purchase of a Boeing 737 flight simulator, at an estimated total cost of $3,500,000. The Province of Nova Scotia has agreed to provide a grant of up to $3,400,000 toward the cost of these facilities. To December 31, 1975 advance payments totalling $1,664,802 have been made by Eastern Provincial of which $1,189,144 has been refunded pursuant to this agreement. The balance of $475,658 has been included in current assets under "Receivables".

8. Government Subsidies

Certain of the routes serviced by Eastern Provincial are eligible for federal subsidies. The Canadian Transport Commission has confirmed that the same routes which were eligible for subsidies in 1974 are eligible in 1975, but has restricted the amount of the 1975 subsidy allotment to $1,700,000 regardless of the cost of providing these services. Accordingly, although Eastern Provincial has submitted a claim of $2,289,000 for providing these services in 1975, only $1,700,000 has been recorded of which $500,000 was receivable as of December 31, 1975 (1974 - $922,265) and is included in current assets under "Receivables".

9. Overhaul Provisions

Prior to 1975, Eastern Provincial provided for major airframe overhaul costs on the basis of aircraft flying time. As a result of the commencement, during 1975, of a program of continual in-house airframe maintenance, no liability provisions to outside agencies are required and the accumulated provision as of December 31, 1974 of $486,700 has been credited to operating expenses which has served to reduce the basic loss per Common share by $0.21.

10. Anti-Inflation Regulations

The Company and its subsidiaries are subject to restrictions on prices, profits, dividends and compensation under the Anti-Inflation Act.

11. Remuneration of Officers and Directors

The aggregate remuneration paid by the Company and its subsidiaries to its directors and senior officers for the year ended December 31, 1975 was $331,000 (1974 - $351,000).

12. Comparative Figures

Certain figures for 1974 have been reclassified to conform with the current year's presentation.

	1975	1974	1973	1972	1971
Financial ($000's)					
Revenues					
Scheduled Passengers	$24,983	$22,637	$17,914	$13,304	$11,960
Cargo	3,991	3,550	2,750	2,551	2,193
Government Subsidies	1,700	1,725	1,753	1,717	1,391
Charter & Other	5,228	2,911	746	1,382	1,070
	$35,902	$30,823	$23,163	$18,954	$16,614
Expenses					
Operating	$32,222	$26,282	$17,933	$14,470	$12,982
% of Revenues	89.7%	85.3%	77.4%	76.3%	78.1%
Depreciation, Aircraft Rentals& Interest	$ 5,766	$ 4,177	$ 3,438	$ 2,840	$ 3,416
% of Revenues	16.1%	13.6%	14.8%	15.0%	20.6%
Deferred Income Taxes	$(342)	$ 342	$ 1,111	$ 958	$ 117
(Loss) Earnings Before Extraordinary Items	$(190)	$ 506	$ 1,111	$ 981	$ 155
Per Common Share	$(0.27)	$ 0.37	0.88	$ 0.97	$ 0.15
Net (Loss) Earnings	$(190)	$ 506	$ 1,111	$ 981	$ 1,618
Per Common Share	$(0.27)	$ 0.37	$ 0.88	$ 0.97	$ 1.62
Funds (Applied To) Provided From Operations	$(405)	$ 2,654	$ 3,084	$ 2,720	$ 2,266
Per Common Share	$(0.45)	$ 2.16	$ 2.52	$ 2.69	$ 2.27
Other Statistics					
Scheduled Operations					
Passengers Carried	604,000	594,000	539,000	377,000	332,000
Pass. Miles Flown (000)	238,000	239,000	216,000	160,000	143,000
Yield per Passenger Mile	10.5c	9.5c	8.3c	8.3c	8.4c
Cargo Ton Miles (000)	3,799	3,810	3,659	3,460	3,066
Yield perCargo Ton Mile	$ 1.05	$ 0.93	$ 0.75	$ 0.74	$ 0.72
Total Revenue Ton Miles (000)	27,575	27,666	25,264	19,461	17,402
Capacity Ton Miles (000)	51,532	52,053	47,270	36,933	33,589
Revenue Weight Load Factor	53.5%	53.2%	53.4%	52.7%	51.8%
Employees at Year End	771	752	640	521	510
Revenue Ton Miles per Employee	35,800	36,800	39,500	37,400	34,100

Glossary of Terms

CAPACITY TON MILES

Number of tons capacity for the carriage of passengers and cargo multiplied by the number of miles this capacity is flown. A measure of aircraft capacity offered.

CARGO

Freight, express, mail and excess baggage.

CARGO TON MILES

Tons of freight, express, mail and excess baggage carried multiplied by the miles they are flown.

REVENUE PASSENGER MILES

Total revenue passengers carried multiplied by the number of miles they are flown.

REVENUE TON MILES

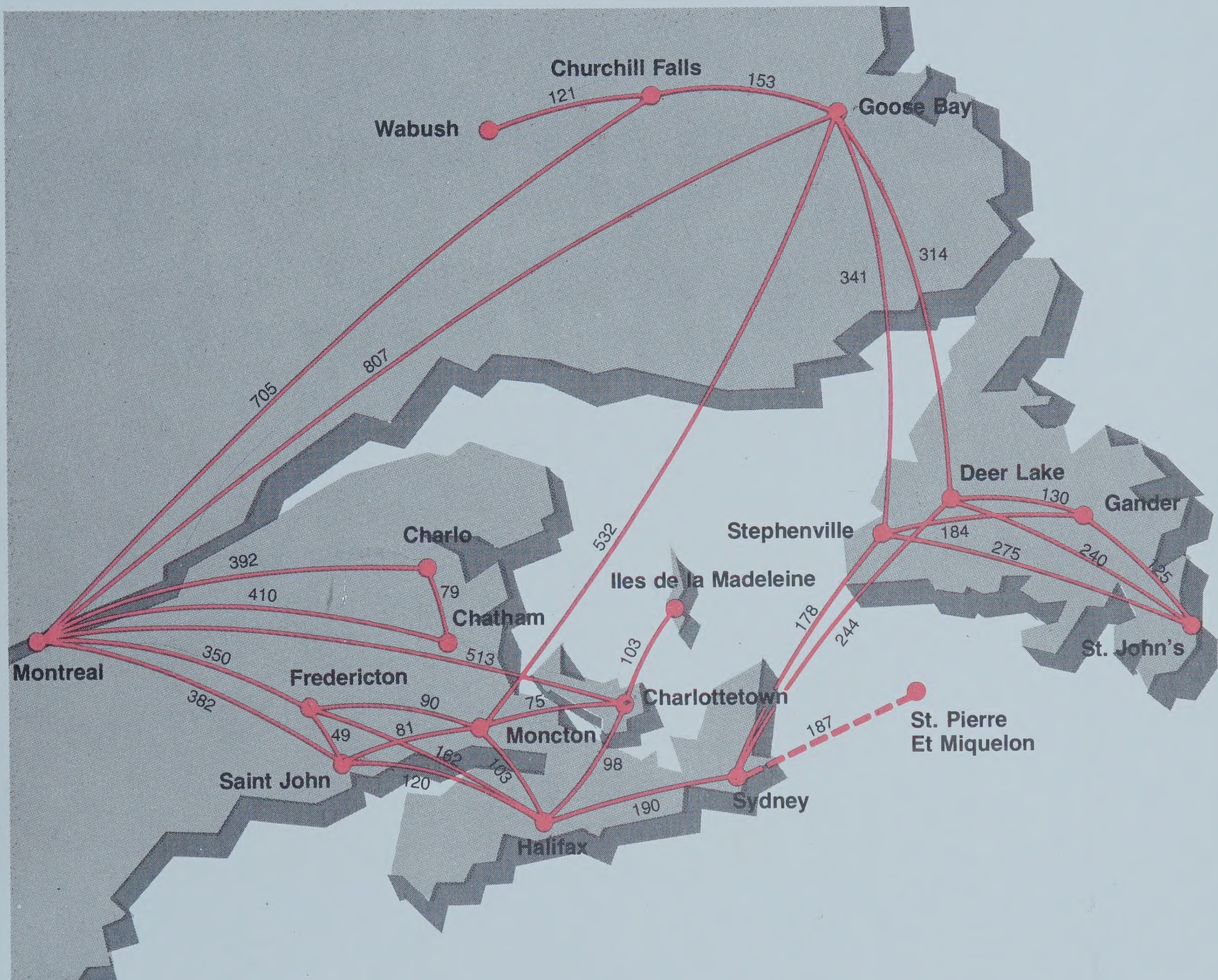
Total tons of all revenue traffic carried multiplied by the miles they are flown.

REVENUE WEIGHT LOAD FACTOR

Total revenue ton miles as a percent of the capacity ton miles.

YIELD

The average revenue per revenue passenger mile or revenue ton mile.


Churchill Falls
Wabush
121
153
Goose Bay
705
807
341
314
532
Charlo
392
410
79
Chatham
Iles de la Madeleine
Montreal
350
382
513
Fredericton
90
75
Charlottetown
103
49
81
Moncton
162
103
98
Saint John
120
190
Halifax
Sydney
187
St. Pierre
Et Miquelon
178
244
Stephenville
Deer Lake
130
Gander
184
275
240
125
St. John's

EASTERN PROVINCIAL AIRWAYS
Growing with Atlantic Canada.

Head Office: Gander, Newfoundland

EASTERN PROVINCIAL AIRWAYS LIMITED AND SUBSIDIARY COMPANIES

Consolidated Statement of Source and Application of Funds

FOR THE SIX MONTHS ENDED JUNE 30, 1975
(With Comparative Figures for 1974)
(Unaudited)

	1975	1974
	(in thousands of dollars)	
FUNDS PROVIDED BY		
Operations:		
Net Earnings (loss) for the period	(160)	$ 73
Non-Cash Charges Against Earnings - Net	138	926
Funds Provided From (applied to) Operations	(22)	999
Long Term Borrowings	83	-
Sale of Fixed Assets	8,256	10
Preferred Share Issue	1,020	-
Total Funds Provided	9,337	1,009
FUNDS APPLIED TO		
Property and Equipment		
- Aircraft and Spares	1,692	552
- Other	558	429
Long Term Debt	4,928	723
Investments	293	-
Dividends	53	150
Pre Operating Expenses	628	-
Redemption Preferred Shares	27	-
Total Funds Applied	8,179	1,854
INCREASE (DECREASE) IN WORKING CAPITAL	$1,158	$ (845)

Comparative Highlights

FOR THE SIX MONTHS ENDED JUNE 30, 1975

	1975	1974
EARNINGS:		
Revenue — Gross	$16,754,000	$13,921,000
Net Earnings (loss)	$ (160,000)	$ 73,000
Net Earnings (loss) per share	$ (0.18)	$ 0.04
FINANCIAL POSITION:		
Working Capital	$ 2,773,000	$ 1,413,000
Property & Equipment	$16,894,000	$16,722,000
Shareholders' Equity	$ 7,579,000	$ 6,515,000
Equity per Common Share	$ 4.65	$ 4.59
SCHEDULED OPERATIONS:		
Passengers Carried	273,062	271,072
Cargo Ton Miles	1,834,379	1,880,356
Revenue Ton Miles	12,576,234	12,678,478
Capacity Ton Miles	24,380,829	24,738,868
Revenue Weight Load Factor	51.6%	51.3%

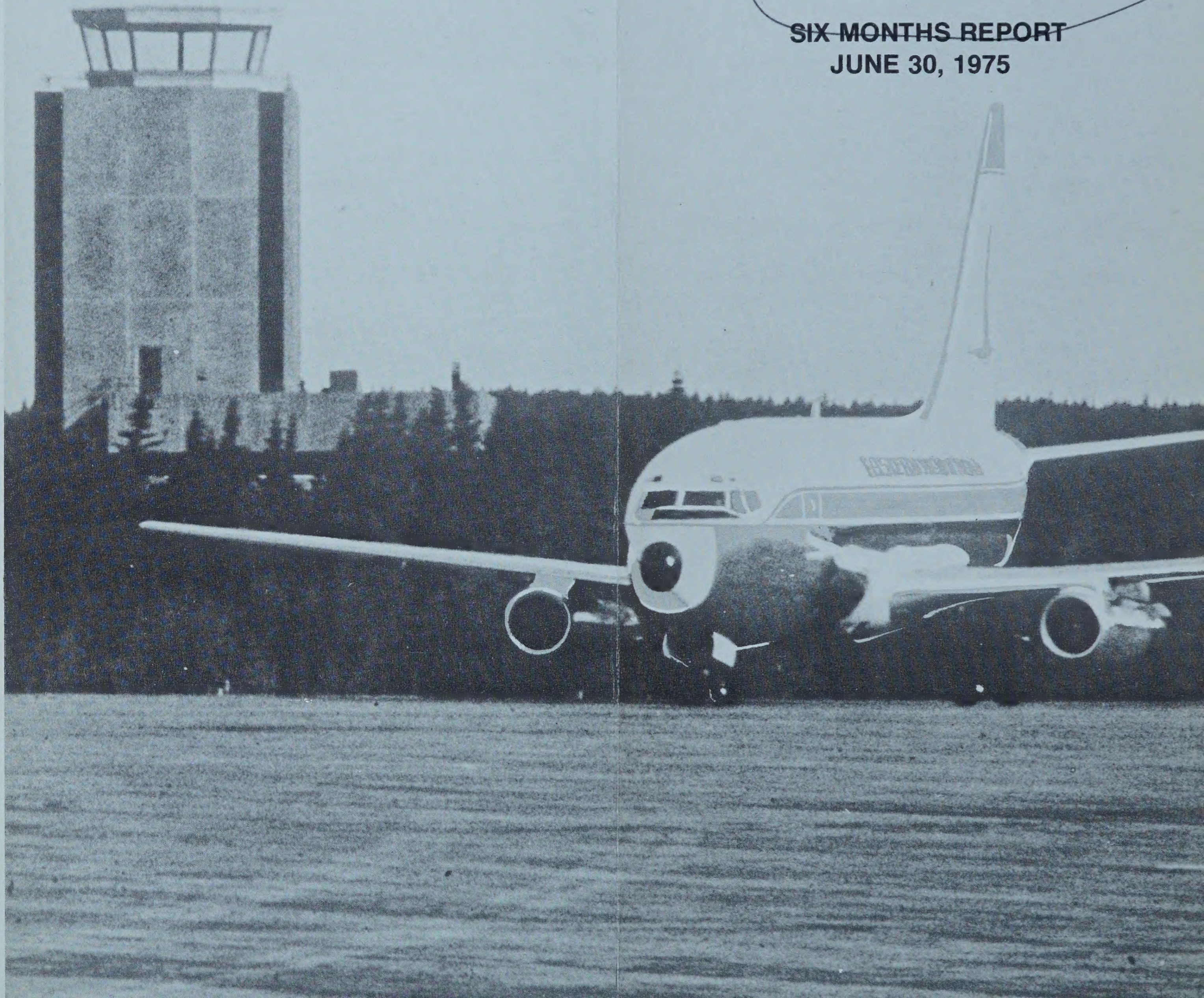
EASTERN PROVINCIAL AIRWAYS

Head office: Gander, Newfoundland

File

EASTERN PROVINCIAL AIRWAYS

SIX MONTHS REPORT
JUNE 30, 1975



PRESIDENT'S REPORT

TO THE SHAREHOLDERS:

The soft demand for air travel and inflationary cost pressures which were experienced during the first quarter of the year continued to affect the Airline during the second quarter. An increase in passenger fares requested in April was approved, substantially in its entirety, and became effective June 1. This increase assisted in the improvement in operating results for the second quarter.

The net loss before extraordinary items for the first half was $584,000 or 53c per share compared to a profit of $73,000 or 4c per share for the comparative period in 1974. After an extraordinary gain of $424,000 the net loss for the first half of 1975 was $160,000 or 18c per share.

The number of passengers carried on scheduled services during the first six months was practically the same as last year. The series of rotating strikes by Federal Airport employees had an adverse effect on air travel in the first quarter. In all total traffic volume on scheduled services was down approximately one percent from last year. Despite this decline the Airline was able to improve its load factor by optimizing the mix of aircraft availability between scheduled and charter services.

During the period under review the financial position of the Company was improved by the issue of $1,020,000 Series "B" 10¾% Redeemable Preference Shares and the refinancing of a Boeing 737 aircraft. The refinancing of the aircraft, through a sale and lease-back arrangement, improved working capital by an amount in excess of $1,500,000 and gave rise to a gain of $424,000 which is shown as an extraordinary item on the Income Statement.

Wage contracts for two years duration have been negotiated with Unions representing the Engineering, Clerical, Traffic and Reservations Agents. These settlements call for wage increase ranging from 13-17% during the first year and 9-10% plus a cost of living allowance during the second year. Negotiations with the Pilots Association are presently in progress and negotiations will commence with the Stewardess and Flight Dispatch groups in the autumn.

Detailed studies into a subsidiary system of local air service within the Atlantic Region have now been completed and submitted to the Governments of the four Atlantic Provinces and the Federal Government for review and approval. The results of these discussions will determine whether or not a firm purchase commitment for three DeHavilland Dash 7 aircraft will be signed.

The establishment of a centralized training and base facility for flight crews at Halifax is proceeding well. Progress payments have been made on the Boeing 737 simulator and final designs for the housing of the simulator and hangar requirements have been agreed upon. The target date for completion and operation of these facilities is late 1976.

Financing for the seventh Boeing 737 aircraft, being delivered in November of this year, has been arranged with a Canadian Bank and the U.S. Export-Import Bank. This aircraft will make it economically viable for the Airline to perform, in-house, major B737 airframe overhauls which are presently being contracted out to another carrier. During the coming winter season the aircraft will be actively utilized in the Southern Charter Service.

Traditionally the first half of the year has been a low period for the Company's earnings. 1975 to-date has been a most difficult period resulting from no real traffic growth on scheduled services and escalating costs for labor and materials. While it was expected that the traffic demand would be more bouyant in the second half of the year, it is anticipated now that normal growth will not take place until next year. Certainly the Lower Churchill Hydro Development and Off-Shore Oil Exploration in Labrador will be added stimuli in 1976. In the meantime traffic projections have been revised downward, measures are being taken to reduce costs and to obtain the optimum utilization of the aircraft fleet and facilities so that the viability of the Airline will be maintained.

K. A. Miller

K. A. Miller
President and Chief Executive Officer
August 8, 1975

EASTERN PROVINCIAL AIRWAYS LIMITED AND SUBSIDIARY COMPANIES

Consolidated Statement of Earnings
FOR THE SIX MONTHS ENDED JUNE 30, 1975
(With Comparative Figures for 1974)
(Unaudited)

(in thousands of dollars)	1975	1974
REVENUE:		
Scheduled Operations	$12,937	$11,335
Government Subsidies — 1975 Estimated	1,100	730
Charter and Other	2,717	1,856
	16,754	13,921
EXPENSES:		
Operating	16,431	12,982
Depreciation and Amortization	930	655
	17,361	13,637
EARNINGS (LOSS) FROM OPERATIONS	(607)	284
OTHER INCOME	297	242
	(310)	526
INTEREST AND DEBT EXPENSE	781	529
EARNINGS (LOSS) BEFORE INCOME TAXES AND EXTRAORDINARY ITEM	(1,091)	(3)
DEFERRED INCOME TAX PROVISION (REFUND)	(507)	(76)
NET EARNINGS (LOSS) BEFORE EXTRAORDINARY ITEM	(584)	73
EXTRAORDINARY ITEM — NET OF DEFERRED TAXES	424	-
NET EARNINGS (LOSS)	$ (160)	$ 73
BASIC EARNINGS (LOSS) PER SHARE BEFORE EXTRAORDINARY ITEM	(.53)	.04
BASIC EARNINGS (LOSS) PER SHARE	(.18)	.04

Consolidated Statement of Retained Earnings
FOR THE SIX MONTHS ENDED JUNE 30, 1975
(With Comparative Figures for 1974)
(Unaudited)

(in thousands of dollars)	1975	1974
RETAINED EARNINGS BEGINNING OF PERIOD	$4,141	$3,924
NET EARNINGS (LOSS) FOR THE SIX MONTHS	(160)	73
REALIZATION OF EXCESS OF APPRAISED VALUE OF PROPERTY AND EQUIPMENT OVER COST	5	5
	3,986	4,002
DIVIDENDS		
PREFERRED SHARES	53	30
COMMON SHARES	-	120
RETAINED EARNINGS END OF PERIOD	$3,933	$3,852